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IN THE

Supreme Court of the United States

OCTOBER TERM, 1934.

IN THE MATTER OF

THE CHICAGO, ROCK ISLAND & PACIFIC RAILWAY COMPANY,

Debtor.

Nos. 479-488:

CONTINENTAL ILLINOIS NATIONAL BANK & TRUST COMPANY, *et al.*,

Petitioners,

v.

THE CHICAGO, ROCK ISLAND & PACIFIC RAILWAY COMPANY, *et al.*,

Respondents.

Nos. 489-490:

RECONSTRUCTION FINANCE CORPORATION,

Petitioner,

v.

THE CHICAGO, ROCK ISLAND & PACIFIC RAILWAY COMPANY, *et al.*,

Respondents.

BRIEF OF RESPONDENTS IN OPPOSITION TO PETITIONS FOR WRITS OF CERTIORARI.

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Opinions Below.

No opinion was rendered by the District Court.

The opinion of the Circuit Court of Appeals (R., pp. 313-326) is reported in 72 F. (2d) 443.

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BRIEF OF RESPONDENTS IN OPPOSITION TO PETITIONS FOR WRITS OF CERTIORARI.

This Court should deny the petitions for writs of certiorari because the decisions of the Courts below were clearly right and were based on facts found by the District Court and sustained by the Circuit Court of Appeals, which this Court does not review.

In order to make it appear that there are involved broad questions of general application which should be reviewed by this Court, the petitioners have distorted and enlarged one question involved in this case and have tried to make much of a procedural question and a constitutional question which are without substance.

The very statement in the petitions of the one question argued by all the petitioners is incorrect in that the decisions below were much more limited than the statement indicates. For example, the Reconstruction Finance Corporation makes it appear that the question is the broad one whether, in a proceeding under Section 77 of the Bankruptcy Act [11 U. S. C. A., §205], the Court generally may enjoin the sale by pledgees of collateral irrespective of its nature and amount and irrespective of the effect of the sale on the proceeding. The decisions below stand for no such general principle.

It was never contended in either of the Courts below that, in a proceeding under Section 77, the Court has general power to enjoin the sale of collateral by pledgees irrespective of the nature or amount of the collateral or the effect of the sale thereof upon the proceeding. It was contended below simply that in a proceeding under Section 77 the Court should examine the particular circumstances of each case,—that is, the amount and nature of the collateral, the size of the loan, and the particular capital and debt structure of the railroad system—to decide whether or not the sale or threat of sale of the collateral would, in effect, prevent a reorganization of that particular railroad system. The District Court made such an examination in this case and found that under the particular circumstances of this case the issuance of the injunction order was necessary to

preserve the sole purpose of the proceeding and, accordingly, issued the injunction.

The opinion of the Circuit Court of Appeals, affirming this decision, shows that the question was the narrow one of determining the necessity for the issuance of the injunction under the particular circumstances of this case (R., pp. 323-324):

> "The consummation of a fair and equitable plan of reorganization is the goal of the legislation. How could a plan of reorganization be perfected unless the courts restrained creditors and lienholders from proceeding in a manner which would defeat the consummation of said plan?
>
> "In the instant case some fifty-four millions of dollars of the debtor's and its subsidiaries' bonds were hypothecated with creditors whose claims were scarcely one-third that amount. To successfully reorganize, it is necessary to take care of the funded indebtedness amounting to approximately two hundred and eighty millions of dollars. If, in addition thereto, fifty-four million dollars of bonds were beyond the control of the court, **it would be quite impossible to proceed with any reorganization.**"

In view of the finding that the issuance of the injunction was necessary to permit a reorganization to be effected and to carry out the sole purpose of the proceeding under Section 77, the inevitable decision of the courts below was to issue and sustain the injunction. Any other decision would have nullified the purpose of Congress in enacting Section 77 for the reorganization of railroads. Obviously, this Court would reach no other result and a review of that question here would serve no real purpose.

There was no dissent below and no different view has been expressed in any other circuit. On the contrary, a District Court in the Ninth Circuit has issued an injunction on similar grounds in a proceeding under Section 77B [11 U. S. C. A. §207] (which is analogous to Section 77 but applicable to corporations other than railroads). *In re White Truck & Transfer Co.* (U. S. D. C., S. D., Cal.), Par. 3006, Commerce Clearing House Bankruptcy Service, p. 1107.

It should also be pointed out that the opinion of the Circuit Court of Appeals, as well as the findings contained in the order of the District Court, are very definite and clear and would leave no reader in doubt as to the limited nature of the question decided. Therefore there is no necessity for a review to clear up any ambiguity in the decision or limit its application.

The procedural question, argued only by three of the Banks, will be shown to have no important bearing. The constitutional question, argued only by the Banks, will be shown to be clearly "untenable," as held by the Circuit Court of Appeals.

I. A Statement of the Facts.

The petitioners are not in a position to dispute the findings of fact contained in the order of the District Court and affirmed by the Circuit Court of Appeals. For it was stipulated in open court that the petitioners might contest the merits of the application without waiving their special appearances (R., p. 119) and they submitted no evidence whatever (See Statement of Evidence, R., pp. 111, *et seq.*). Accordingly, for all purposes of any appeal and this peti-

tion, the facts set forth in the papers supporting the application in the District Court must be taken as undisputed.

The undisputed facts upon which the order was based are as follows:

On June 7, 1933, the Chicago, Rock Island and Pacific Railway Company initiated the proceeding under Section 77 of the Bankruptcy Act, in which a number of the subsidiary railroad companies of the System shortly thereafter joined, all for the sole purpose of effecting a plan of reorganization of the Rock Island System* (R., pp. 2-5, 26-28, 92-96).

At the time the reorganization proceeding began, the Debtor was indebted on relatively long-term promissory notes (most of them for 19 months) to the petitioners, Reconstruction Finance Corporation and the Banks, in the total sum of approximately $17,784,000, which was secured by mortgage bonds in the approximate aggregate face amount of $54,000,000. These bonds are either primary obligations of the principal Debtor, The Chicago, Rock Island & Pacific Railway Company, or obligations guaranteed by the principal Debtor, or obligations of System railroad companies which have also become Debtors in this same proceeding, or obligations of subsidiaries of the principal Debtor, and all are secured by lien upon some

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* That the sole purpose of this proceeding under Section 77 is to effect a reorganization of the Rock Island System is clear from a reading of the first sentence of Section 77, subdivision (a), and also from Clause 7 of subdivision (c) of Section 77, which provides that if a plan of reorganization is not proposed, accepted and confirmed within a reasonable time, the Court may dismiss the proceeding.

part of the Debtor Railroad System (R., pp. 12, 13, 14, 37, 38, 39, 67, 92, 93, 94).*

Under the provisions of the collateral notes held by the petitioners, the right of sale of the collateral existed at the time the application was made, and the danger of sale was imminent (R., p. 103).

It appeared that if this $54,000,000 total face amount of collateral were sold at the time, it would not yield the face amount of the notes, which was only one-third the amount of the collateral, namely, approximately $17,000,000, and might even result in a deficiency on the notes (R., p. 40). Consequently, following the sale there would be outstanding, in place of this $17,000,000 of claims, claims against the Debtor's estate totaling $54,000,000, *plus* any deficiency in the price brought by the collateral below $17,000,000. Thus, this particular indebtedness of the System would be more than tripled.

Furthermore, other creditors of the System held collateral, also consisting of obligations secured by mortgage liens upon the System or capital stock of other System companies, in the additional principal amount of $145,749,050 which would also become subject to sale because of the existence of events of sale in the indentures under which such collateral was held as security (R., p. 66). It was pointed out to the District Court that a decision that the Reconstruction Finance Corporation and the Banks should not be enjoined from selling the $54,000,000 face amount of collateral held by them, would also determine that such $145,749,050 of other collateral was free for sale,

* There is one minor exception,—among the collateral held by the Reconstruction Finance Corporation is the Rock Island's claim against the Railroad Credit Corporation in the face amount of approximately $1,400,000 (R., p. 38).

making a total of $200,000,000 of capital obligations of the System not now outstanding as primary debts but which would then be free for sale at a fraction of face value (R., p. 67).*

It further appeared that the total outstanding capitalization of the System was approximately $459,000,000, consisting of funded debt in the amount of $312,365,720, bank loans in the amount of $17,843,700, and stock in the amount of $128,909,211 (R., pp. 87-88). It was obvious that a plan of reorganization which would take care of a readjustment of an outstanding capitalization of $459,000,000 would not take care of an outstanding capitalization of from $600,000,000 to $650,000,000, which would result from sales of all or portions of the $200,000,000 total of capital obligations of the System held as collateral. Moreover, such sales might take place from time to time while attempts were being made to prepare a plan of reorganization, obtain assents thereto and put it into effect. Each sale would require a modification of the plan, result in a change in the number and classes of claimants theretofore fixed by the Court, whose assents must be obtained to the plan, and nullify any proceedings or assents on the plan theretofore taken.

No attack was made on the validity of the pledges of collateral or on the substantive rights of the pledgees or on the position to be accorded the pledgees in the plan of reor-

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* Notwithstanding that $141,739,050 of the above collateral secured the two bond issues represented by the Protective Committee for the Debtor's First and Refunding Bonds and Secured 4½% Gold Bonds, that Protective Committee supported the application for the injunction in the District Court, argued for sustaining the injunction on appeal in the Circuit Court of Appeals, and in this brief opposes these petitions for writs of certiorari (R., pp. 65-68).

ganization on account of their holding this large amount of collateral; and no relief was applied for which would do more than delay the use by the pledgees of their remedies. The point was that if no sale of the collateral took place the Rock Island, in order to take care of these claims, would not have to provide in the plan of reorganization cash or new A-1 securities in an amount in excess of the primary debt of $17,000,000 due to the pledgees. On the other hand, if the pledgees were to be permitted to sell their collateral, the Rock Island would have to provide in the plan for over $50,000,000 of new securities of various types to take care of these collateral securities which would then become outstanding primary debts. Also the trustees for bond issues of the Debtor holding similar collateral would be free to sell such collateral and the Rock Island would have to provide new securities of various types to take care of the $145,000,000 of such collateral not presently outstanding as primary debts. In addition sales would result in the mechanical obstacles to reorganization already mentioned.

Following oral argument and submission of briefs by the Banks, the R. F. C. and the other parties, the District Court found and determined, and so stated in its order, (a) that the facts set forth in the petition and the supporting affidavit were true, (b) that the sale of the collateral would in effect prevent the orderly preparation and consummation of a plan of reorganization under Section 77, which is the sole purpose of Section 77, (c) that it was necessary for the enforcement of the provisions of Section 77 that such sale be enjoined pending the preparation and consummation of a reorganization plan, and (d) that the Court had power under clause (15) of Section 2 of the Bankruptcy Act [11 U. S. C. A., §11 (15)] to make such orders,

in addition to those specifically provided for in the Act, as might be **necessary** for the enforcement of the Act (R., pp. 103, 104). Accordingly, the Court entered the injunction order pursuant to such findings (R., p. 104).

The findings of fact of the District Court could not be reversed on appeal unless determined to be clearly wrong. The Circuit Court of Appeals held not only that the findings of fact by the District Court were not clearly wrong, but that they were right, saying:

> "Upon the record before us we cannot say that the sale of the collateral by the pledgees will not defeat the purposes of Section 77. On the other hand, we agree with Judge Wilkerson that the facts called for an exercise of discretion on the part of the court in favor of the moving parties". (R., p. 324).

II. There Are No Questions Which Can Be Raised on this Record Which Warrant Review by this Court.

QUESTION 1. One question is argued by both petitions. But, as already stated, this question is not the broad one indicated by the petitioners as to the power of a Bankruptcy Court in a proceeding under Section 77, generally to enjoin the sale by pledgees of collateral of whatever nature and amount and under any circumstances. It is the limited one whether the Bankruptcy Court, in a proceeding under Section 77 for the reorganization of a railroad system, has the power to enjoin the sale of collateral consisting of capital obligations of the Debtor Railroad System in large amounts greatly exceeding the primary debt, where the Court finds under the particular circumstances of the case that the sale

of the collateral would prevent the preparation and carrying out of a plan of reorganization of the System, which is the sole purpose of the proceeding.

This question does not warrant review by this Court because the decisions of the Courts below were obviously correct. This Court will certainly not disturb the findings of fact made by the Courts below, namely, that in the particular circumstances of this case the issuance of the injunction was necessary to carry out the sole purpose of the proceeding, that is, reorganization of the Rock Island System. The necessity for the issuance of the injunction order to preserve the proceeding having been conclusively established, the only question remaining is whether the Court had power to issue the necessary order. But, the Court having found that the issuance of the order was **necessary** to prevent the proceeding from becoming abortive, the Court had the power to make the order under the express provisions of the Bankruptcy Act itself. For Section 2 of the Bankruptcy Act [11 U. S. C. A., §11] provides:

> "The courts of bankruptcy * * * are hereby invested, within their respective territorial limits as established on July 1, 1898, or as they may be hereafter changed, with such jurisdiction at law and in equity as will enable them to exercise original jurisdiction in bankruptcy proceedings, * * * to * * * (15) make such orders, issue such process, and enter such judgments in addition to those specifically provided for as may be **necessary** for the enforcement of the provisions of this title."

However, the petitioners argue that notwithstanding the presence of this section in the Bankruptcy Act the Court had no power to make the injunction order, even though

necessary for the enforcement of the Act. Petitioners contend that prior to the enactment of Section 77, the weight of authority was that injunctions would not be issued against the sale of collateral by pledgees in an ordinary bankruptcy proceeding, and that such decisions, therefore, show that the power to issue such injunctions does not exist under Clause (15) of Section 2.

However, this contention completely loses sight of the fact that the power to issue an order pursuant to Clause (15) of Section 2 flows only from the **necessity** of issuing the order for the enforcement of the Bankruptcy Act. If there is no such necessity there is no such power. And the complete answer to petitioners' contention is that prior to the enactment of Section 77 as part of the Bankruptcy Act there was no necessity for enjoining the sale of collateral by pledgees in most cases in order to carry out the purposes of the ordinary bankruptcy proceeding. The primary purpose of bankruptcy proceedings prior to the enactment of Section 77 was to effect an **orderly liquidation** of the business and property of the bankrupt and an **equitable distribution** among its creditors. The sale of collateral by those holding notes of the bankrupt in the ordinary case would facilitate and hasten, rather than prevent, liquidation and distribution among the creditors according to their respective rights.

Since, in the usual case in ordinary bankruptcy, the sale of collateral would facilitate the carrying out of the purposes of the proceeding, there could be no necessity for enjoining the sale to preserve the purposes of the proceeding.

However, the sole purpose of a proceeding under the new Section 77 of the Bankruptcy Act is to **reorganize** the

Debtor, not to liquidate its business and property and make a distribution among its creditors. The difference between the purposes of an ordinary bankruptcy proceeding, *i. e.*, **liquidation and distribution**, and the purpose of a proceeding under Section 77, *i. e.*, **reorganization**, is well stated by the Circuit Court of Appeals in its decision in this case:

> "That which distinguishes this section [77] from the old act—the gist of the change evidenced by this amendment, that which makes it effective—is the provision which calls for a plan of reorganization. It calls not for a sale of assets and a discharge of the debtor, but for a plan of reorganization wherein the indebtedness and capital structure are changed (usually reduced) so that the debtor may live and the creditors will receive more than is obtainable upon a liquidation sale. The consummation of a fair and equitable plan of reorganization is the goal of the legislation" (R., p. 323).

The purposes of the two types of proceedings being so different, the Circuit Court of Appeals was plainly right in holding that any consideration of the cases under the old bankruptcy procedure was unnecessary. On this point the Circuit Court of Appeals said:

> "That the order may have been sustained under the Bankruptcy Act, before amendment under certain circumstances and as against creditors who occupy positions similar to some of the appellants is earnestly asserted. We are, however, for brevity's sake, avoiding a discussion of such questions because unnecessary. We desire to direct our attention to the statute as amended—to the condition that confronts us, not to a theoretical or supposititious question." (R., pp. 320, 321.)

Accordingly, the cases cited by the petitioners as representing the weight of authority against enjoining the sale of collateral consisting of obligations of the bankrupt in ordinary bankruptcy proceedings prior to the enactment of Section 77 are wholly inapplicable.*

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* The only case cited by petitioners in which an injunction against the sale of collateral consisting of obligations of the bankrupt was denied in an ordinary bankruptcy proceeding is *In re Ironclad Mfg. Co.*, 192 Fed. 318 (C. C. A. 2d, 1912).

The other cases cited by the petitioners as showing that Bankruptcy Courts, prior to the enactment of Section 77, did not enjoin the sale of collateral are readily disposed of as not even standing for that proposition.

Jerome v. *McCarter*, 94 U. S. 734, 739 (1876), was a case involving an equity receivership, and the sale of collateral discussed by the Court there took place before the equity receivership and during a prior bankruptcy, in which no injunction against the sale of the collateral had been applied for. The Court simply said that the sale having taken place the purchaser could prove on the bonds in the equity receivership.

In *Hiscock* v. *Varick Bank of New York*, 206 U. S. 28 (1907), the collateral consisted of obligations of a third party, and the sale having already taken place, no question of injunction was involved.

In *Turner* v. *Metropolitan Trust Co.*, 207 Fed. 495, 499 (C. C. A. 9th, 1913), the sale of the collateral took place before the bankruptcy, and the case of *Rogers Brown & Co.* v. *Tindel Morris Co.*, 271 Fed. 475, 476 (D. C., E. D. Pa., 1921), was an equity receivership and involved no question of the powers of a Court of Bankruptcy.

In *Worth* v. *Marshall Field & Co.*, 240 Fed. 395 (C. C. A. 4th, 1917), no question of a sale of collateral or of an injunction was in any way involved.

In *In re Hudson River Navigation Corp.*, 57 F. (2d) 175 (C. C. A. 2d, 1932), the collateral consisted almost entirely of notes which were obligations of third parties.

The one case cited by petitioners which really stands for the proposition for which it is cited (the *Ironclad* case) is not made applicable to a reorganization proceeding under Section 77 by subdivision (n) of Section 77, briefly mentioned by the petitioners. Subdivision (n) of Section 77 simply grants to a court which is proceeding under Section 77 the general powers which a Bankruptcy Court had under the old Bankruptcy Act so far as such grant is "consistent with the provisions" of Section 77. This grant of power cannot be twisted into a limitation of power, or in any event into such a limitation of power as would be inconsistent with the purposes of Section 77.

Moreover, even in an ordinary bankruptcy proceeding, before the enactment of Section 77, injunctions against the sale of collateral were issued when found necessary in order to carry out the purposes of such proceeding, namely, orderly liquidation and distribution.

Thus, in *John Matthews, Inc.* v. *Knickerbocker Trust Co.*, 192 Fed. 557 (C. C. A. 2d, 1911), the Court issued an injunction against the sale of collateral consisting of unsecured obligations of the bankrupt itself, because the sale would have prevented *pro rata* distribution among the creditors, would consequently have prevented the accomplishment of the purpose of an ordinary bankruptcy proceeding, and therefore the issuance of an injunction was necessary to enforce the Act. In sustaining the injunction, the Circuit Court of Appeals said (p. 558):

> "Any rule which would permit the proof of two notes for one indebtedness would permit the proof of a dozen and would substitute for *pro rata* distribution among real creditors distribution in accordance with the ability of a bankrupt to make manifold obligations for single debts."

The authority of this case has never been questioned in this proceeding or in any other case. The power to issue such an injunction was derived from the **necessity** of issuing it to preserve the purpose of the proceeding. It follows that such necessity gave the Court the power, even under the old Bankruptcy Act, to enjoin the sale of collateral under Clause (15) of Section 2.

The petitioners have not called to the attention of the Court any authorities which indicate that the express language of Clause (15) of Section 2 of the Act is not to

be given its plain force and effect, namely, that a court of bankruptcy has the power to issue any order which it finds necessary under the facts of a particular case to carry out the purpose of a proceeding under the Bankruptcy Act, whether ordinary bankruptcy or reorganization under Section 77. As previously stated herein, the District Court and the Circuit Court of Appeals have found that the issuance of the injunction order was necessary under the particular facts of this case to carry out the sole purpose of this proceeding under Section 77 for the reorganization of the Rock Island System. Accordingly, there can be no question but that the Court had power to issue the injunction order pursuant to Clause (15) of Section 2 of the Act.*

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* In their endeavor to raise a question for this Court, petitioners attempt to make a point that no express authority for the issuance of an order of this type is found in Section 77 itself. And they call attention to subdivision (l) of Section 77 which was obviously written with the purpose in mind of controlling litigation against the debtor, and which, therefore, incidentally provides for staying litigation to enforce liens. Petitioners cite the maxim *expressio unius est exclusio alterius*, and say that because Congress gave express power to stay judicial proceedings for the enforcement of liens, Congress intended to negative the power to enjoin enforcement of liens by means other than judicial proceedings.

There is a short answer to this argument of the petitioners. Subdivision (l) simply deals with the subject of controlling litigation, including litigation to enforce liens upon the estate, and is a grant of power to the Court to control litigation. A subdivision which constitutes a grant of power in connection with the subject of controlling litigation cannot be stretched by any logical process into a limitation of power in connection with a subject which does not involve litigation. Subdivision (l) simply has nothing to do with injunctional or other orders which do not relate to litigation. It certainly cannot be construed, as contended by the R. F. C., as containing the only injunctional powers of the Bankruptcy Court.

The maxim *expressio unius est exclusio alterius* as applied to Section (l) would mean only that it was not intended that an injunction should issue against the commencement of a judicial proceeding not designed to enforce a lien. But the maxim certainly cannot

SUBSIDIARY QUESTION. This is argued only by the Banks. They contend that the Court had no power to issue an injunction against the sale of their collateral, in a **summary** proceeding such as this one was, as contrasted with a **plenary** suit. They urge that the application for an injunction was an attempt to enforce an **adverse** claim to the pledged property in a summary proceeding. The proposition that adverse claims to property, where the person in possession has more than a colorable right, must be made in a plenary suit has never been questioned. However, the application for this injunction was not the assertion of an adverse claim to the collateral. The contention can be most simply answered in the language of the Circuit Court of Appeals:

> "Nor can we say the appellants, the claimants, occupied such an adversary status that a trial in a plenary suit was necessary. The trustees named by the court in the bankruptcy proceedings were not claiming adversely to appellants. The creditors were not claiming liens or title to property adverse to the trustees. The trustees admit the legality of the security held by the creditors, as well as the validity and amount of the creditors' claims.
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> • • • • • •
>
> "The proceeding involved no adversary contest but merely the pursuit of a remedy." (R., p. 324.)

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be stretched to imply a limitation upon the injunctional power of the Court on subjects other than judicial proceedings.

To argue that, because the right to enjoin is specifically given by subdivision (1) in one class of case, it cannot exist in other and quite different cases, is to argue that the general powers clause, Section 2, Clause (15), is no longer in effect. But that clause was inserted in the statute for the precise purpose of preventing deficiencies of power and miscarriages of the proceedings resulting from the failure of specific sections expressly to state all the powers required by the Court for the purpose of making proceedings under the Act effective.

The issuance of an injunction order of this type is simply an administrative function of the Bankruptcy Court. It could not be the subject of a plenary suit in another court for it is an order made by the Bankruptcy Court to protect its own jurisdiction and the proceeding.

QUESTION 2. The three petitioning Banks, which are not located in the Northern District of Illinois, argue the question whether the District Court for the Northern District of Illinois had jurisdiction to issue an injunction against them.

This procedural point has no important bearing on this case. It raises only the question whether the injunction was properly issued by the District Court in the Northern District of Illinois in the case of these three petitioners, or whether it should have been issued in ancillary proceedings by the District Courts in the districts where these three Banks were located. This is a very minor point of procedure, since these District Courts would, as a matter of course, have followed the decision in the original jurisdiction, and have issued similar injunctions.

The Circuit Court of Appeals dealt adequately with this matter (R., pp. 322, 323), and there can be no doubt as to the correctness of its decision in holding that the collateral was property of the debtor, and that, under Section 77, the District Court in the Northern District of Illinois could issue injunctions against the defendants' interfering with this property in other districts, particularly in view of the express language* of Section 77, and of the obvious intent

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* The fifth sentence of subdivision (a) of Section 77 [11 U. S. C. A., §205(a)] provides:

> "If the petition is so approved, the court in which such order approving the petition is entered shall, during the pendency of the proceedings under this section and for the purposes thereof, have exclusive jurisdiction of the debtor and its property **wherever located.**"

of Congress to do away with ancillary proceedings in the case of railroad bankruptcies. The petitioning Banks themselves state in their brief (p. 20) that the provision of Section 77 set forth in the footnote on the preceding page "obviates the necessity of ancillary bankruptcy proceedings • • •."

As this Court has frequently held, the territorial jurisdiction of the District Court is a matter for legislation by Congress and does not involve any constitutional question. No question is presented here of due process involving lack of proper notice or an opportunity to be heard. The petitioners all received ten days' notice and had full opportunity to be heard and were heard.

QUESTION 3. The five petitioning Banks (but not the R. F. C.) argue that a construction of the Bankruptcy Act, including Section 77, permitting the issuance of this injunction, is in violation of the Fifth Amendment of the Constitution.

This contention is without any substance. Nothing need be added to the statement of the Circuit Court of Appeals on the subject:

> "As to the constitutionality of Section 77 of the Bankruptcy Act, little need be said in addition to what has already been stated, to show this objection is untenable. If the order assailed deals merely with the remedy, as we hold it does, then the amendments violate no provision of the Constitution. That such restraining orders affect the remedy only, see *Allebach* v. *Thomas*, 16 F. (2d) 853. Likewise, legislation which deals with the subject of bankruptcy, that is, legislation for the benefit and relief of creditors and debtors—is not subject to the same constitutional limitations as legislation which deals with

other subjects and which affects contractual rights and obligations of debtors and creditors. The grant of power 'to establish * * * uniform laws on the subject of bankruptcy' was necessarily a grant of power the exercise of which would impair the obligation of contracts. For legislation on the subject of bankruptcy contemplated a discharge of the debtor's debts—which is an impairment of contractual obligations. *Hanover National Bank* v. *Moyses*, 186 U. S. 181." (R., p. 326.)

III. Conclusion.

The petitioners make a few general observations to which we shall briefly refer in concluding.

They assert that a large amount of collateral loans made by governmental agencies and banks to railroads have been affected by the decision herein and that the effect of the decision herein will be to make these agencies and banks unwilling to grant similar loans in the future: Since the decision herein of the courts below is limited to proceedings under Section 77 and is further limited by the particular circumstances of this case, it will obviously affect only a very small portion of the loans referred to by the petitioners. Moreover, there is no sound public policy fostering the practice of managements of railroad corporations making desperate eleventh hour efforts to stave off insolvency proceedings and to stay in control through a reckless pledge of system obligations far exceeding in principal amount the funds received and indebtedness secured. When the point is reached where a railroad corporation can obtain funds only through pledging secured obligations of its own system which in face amount ($54,000,000) are three

times the amount of the loan ($17,000,000), the transaction would appear to be improvident and without due regard to the interests of existing creditors. There is no public policy dictating that railroad managements should have a free field for obtaining money on these terms.

The petitioners also assert that they are injured by having been unable to make a quick realization upon their collateral while in the meantime they have not been receiving interest on their loans and the market value of some of the collateral has declined. But the original long term of the loans and the character and amount of the collateral taken by the petitioners shows that they were not contemplating so-called quick loans on readily marketable securities or relying on a quick realization for their protection. Most of the collateral required by the R. F. C. was unlisted and had no ready market. Both it, and that required by the Banks, was in such large blocks as to make sale difficult and the total face amount required to be given in pledge so excessive as to show it was not of a type customarily taken by banks for really current loans. In addition, it has not been the policy of the R. F. C. merely to make quick loans but on the contrary it was the primary purpose of its creation to furnish funds to institutions as well as railroads on "frozen" collateral having no market. However that may be, the real value of this collateral does not depend upon the fluctuating market value of the bonds, but lies in the value of the System properties upon which such bonds are a lien, and the bonds held as collateral constitute a lien on the System properties in an amount three times the face amount of the loans. Accordingly, the Circuit Court of Appeals was correct in stating that the real position of the petitioners was not injured (R., p. 325).

Furthermore, holders of mortgage bonds have been accorded the same treatment under Section 77. They are not permitted to foreclose and yet they are not receiving interest and, if the System properties behind the collateral held by the Banks and the R. F. C. are declining in value, the properties securing these mortgage bonds are also declining in value to the same extent because they are the same properties. So far as concerns the statement that the banks and the government agencies were surprised to find that their remedy of selling collateral might be enjoined after the enactment of Section 77, the holders of mortgage bonds were equally surprised when they learned that their right to foreclose was to be enjoined under Section 77. And at any rate, it should have been no surprise to the petitioners herein because one of them, Mississippi Valley Trust Company, had previously been enjoined from the sale of similar collateral in the equity receivership of the Missouri, Kansas & Texas Railway.

> *Mississippi Valley Trust Company* v. *Railway Steel Spring Co.*, 258 Fed. 346, 354 (C. C. A. 8th, 1919).

It should be borne in mind that no attack whatever has been made on the validity of the collateral or the position to be accorded the petitioners in the plan of reorganization on account of their holding this large amount of collateral. In fact, petitioners have received approximately $377,000 through distributions on their collateral (R., p. 342).

The petitioners try to deal with the application for the injunction as if it involved a dispute between private litigants, each striving to establish his rights in a fund or to

diminish the other's claims,—that is, as if the holders of the System's outstanding bond issues and the Railway Company itself were attacking the Banks and the R. F. C., to diminish the claims of the latter or in order to take property rights from them.

This is not so. The order in question is purely an administrative and procedural matter and the dispute lies rather between the Federal District Court and the petitioners than between the petitioners and the respondents. The respondents are simply upholding the hands of the Federal District Court in its effort to administer this proceeding for the reorganization of the Rock Island System in such a way that a successful reorganization can take place and the System be placed once more on its own feet. The District Court, which has the onerous task of steering this reorganization proceeding to a successful conclusion and which was fully aware, in view of its background of the proceeding, of the obstacles to a successful reorganization, found and determined that the issuance of the order enjoining the sale of the collateral was necessary for carrying out the purposes of Section 77. The Court therefore issued the injunction order as an administrative measure to clear away a major obstacle to its operation of the reorganization machinery placed in its hands by Congress.

The petitioners have raised no questions which warrant review by this Court. The first question argued by the petitioners has not the general application implied but on the contrary is limited in scope. Their procedural and so-called constitutional questions are insubstantial. The decisions of the Courts below on the record in this case were so clearly right that a review by this Court would result only in affirmance.

Therefore, no useful purpose would be served by granting the writs applied for and it is respectfully submitted that the petitions for writs of certiorari should be denied.

Respectfully,

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